

# James Hardie Prosecution - Implications for Company Directors and Officers

by Robert Cunningham, Managing Partner

### ***ASIC -v- MacDonald (No. 11)*** ***[2009] NSWSC 287***

#### **Implications**

The James Hardie case emphasises the heightened responsibilities of directors and officers under the general law and the *Corporations Act 2001* when they are dealing with any issue likely to have a serious effect on others. Their primary duty is always to the company and they must be aware of the damage they may cause to their company if they do not act with proper care and diligence.

#### **Background**

Directors and other officers of the James Hardie companies have been found liable for breaches of the corporations legislation. They stand to be fined significant amounts for the breaches.

James Hardie was a very large, listed trading company and the particular issue (asbestos claims) was extraordinarily sensitive in the Australian community.

The case set out the duties of directors and officers by reference to existing law. In that sense, it did not break new ground. What was unusual was that the Judge was prepared to find a state of affairs which the directors either could not recollect or swore had not existed. The Judge found they were all 'mistaken' in their evidence.

ASIC took civil penalty proceedings against seven directors, the CEO, the general counsel, the CFO and two companies from the James Hardie group of companies. The proceedings alleged breaches of sections 180(1), 181(1), 995 and 999 of the Corporations Law. Sections 180 and 181 appear in the same form in the current *Corporations Act 2001*. The current equivalent of section 995 is section 1041H and the equivalent of section 999 is section 1041E in the *Corporations Act*.

#### **The Facts**

The facts were extensive because:

- there were 12 defendants and the allegations against each of them needed to be worked through carefully;
- the matter lasted 45 sitting days;
- there were 30 barristers representing various parties; and
- 3237 pages of final submissions were handed to Mr Justice Gzell who heard the matter.

Briefly, the sections are concerned with the following:

- Section 180: care and diligence – directors and other officers.
- Section 181: good faith – directors and other officers.
- Section 1041E: false or misleading statements.
- Section 1041H: misleading or deceptive conduct.

Two companies in the James Hardie group were exposed to claims for compensation for asbestos-related injuries. The management of the company devised a plan to separate the group from these two tainted companies so as to quarantine the rest of the group from future asbestos claims. The group was to set up a fund which would be used to meet the claims.

The proceedings related essentially to:

- announcements and presentations made by the company and its officers in relation to the extent of the fund;

- whether it was likely to cover all claims into the future; and
- the manner in which the fund was to be financed.

ASIC alleged that a draft ASX announcement was approved at a meeting of the board of directors on 15 February 2001 and that it contained a number of statements to the effect that:

- the foundation would have sufficient funds to meet all legitimate asbestos claims;
- that it was fully funded; and
- provided certainty for people with legitimate asbestos claims.

ASIC alleged that those statements were false or misleading and that the directors were in breach of section 180(1) of the Corporations Law. They could not have been satisfied the company had a proper basis for making the assertions of sufficient funding.

## The Decision

ASIC made its case under s.180 (care and diligence – directors and other officers) but failed in relation to s.181 (good faith – directors and other officers). It was successful in making its case for breach of sections 1041E (false or misleading statements) and 1041H (misleading or deceptive conduct).

Sections 180 and 181 of the *Corporations Act* are of wider application than section 1041E and 1041H which relate to financial products and services.

Section 180(1) was in the following terms in February 2001:

*A director or other officer of a corporation must exercise their powers and discharge their duties with the degree of care and diligence that a reasonable person would exercise if they:*

*a. were a director or officer of a corporation in the corporation's circumstances; and*

*b. occupied the office held by, and had the same responsibilities within the corporation as, the director or officer.*

Justice Gzell described the formation of the foundation and the separation of the two asbestos companies from the James Hardie group as "potentially explosive steps".

## Interested Parties

Many people were interested in the manner in which the company dealt with the asbestos claims. Interested parties included:

- the people injured;
- unions;
- creditors of James Hardie group companies;
- shareholders in the group companies; and
- investors generally.

## Conclusion

One or more of the defendants has said they are likely to appeal the decision. Even if the appeals are upheld, the case remains as a caution to directors of all companies. They should ensure they have proper governance regimes in place and that they have proper indemnities from the company and insurance of their liabilities to the extent permitted by law. They should always act honestly and diligently.

***If you have any questions regarding the information contained in this bulletin, please do not hesitate to contact Robert Cunningham or Hugh Esler.***



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